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In the Supreme Court of the United States.

OCTOBER TERM, 1930

No. oo 349

OLD COLONY RAILROAD COMPANY, *Petitioner*,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT AND BRIEF IN SUPPORT THEREOF

J. S. Y. IVINS,
Attorney for
Old Colony Railroad Company,
c/o Brewster, Ivins & Phillips,
Southern Building,
Washington, D. C.

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PETITION

The undersigned on behalf of the Old Colony Railroad Company prays that a writ of certiorari issue to review the final decree of the United States Circuit Court of Appeals for the First Circuit entered in the above-entitled case on June 10, 1931 reversing the decision of the United States Board of Tax Appeals.

QUESTION PRESENTED

Should premiums received by a taxpayer on the sale of long-term corporation bonds issued prior to 1904 (when the taxpayer's accounts were on a cash basis) and outstanding during 1921, be regarded as in any part income accruing in that year, either for the purpose of being treated as taxable income or for the purpose of offsetting

concerns income taxes for the year 1921 which the Commissioner contends are due from the Old Colony Railroad Company.

In 1893 the Old Colony leased its railroad lines to the New York, New Haven and Hartford Railroad Company, under an arrangement whereby the New Haven was to operate the railroad and pay a certain rental, including all taxes. Between 1893 and 1904 the Old Colony issued long-term bonds, which were sold at premiums amounting to $199,528.08. It kept its books on a cash payment basis until compelled by the Interstate Commerce Commission to keep them on an accrual basis.

The question to be solved in the case at bar is whether profit arising from the sale of the bonds may be taken into account in determining the expense to be allowed the Old [fol. 86] Colony as a deduction. If the books were kept on a cash basis the deduction allowable would be the interest paid on the bonds, and only that, as that would be the cash disbursement for the year. The Commissioner contends, however, that the real expense in connection with the payment of the interest on the bonds is the amount of it less an aliquot part of the profit, apportioned to the year 1921, amounting to $6,960.64, as the bonds cost the company less than the amount represented by the rate of interest.

There are no authorities precisely in point, and the decided cases in which somewhat similar questions arose relate to companies whose books were kept on a cash basis. See, for instance, Baldwin Locomotive Works v. McCoach, 221 F. 59; Chicago & Alton R. R. Co. v. United States, 53 Ct. Claims, 41. But there is one decided case which is the converse of the case at bar. In Western Maryland Ry. Co. v. Commissioner, 33 F. (2d) 695, a corporation whose bonds were sold at a discount was allowed to figure the proportionate part of the discount as an expense for the year. The same principle applies to the case at bar. If a corporation is allowed to show a greater expense for a given year by adding a proportionate part of a loss on the sale of bonds, there seems no reason to deny to the taxing authorities the right to show a smaller expense by deducting the proportionate part of a gain on a sale of bonds.

Such a result may seem contrary to the case in this circuit of Commissioner v. Old Colony Railroad Company, 26 F. (2d) 408, which involved a similar state of facts. The deci-

sion was that a profit made in 1904, before the passage of the Sixteenth Amendment to the Constitution of the United States, could not be taxed. The court's attention was not called to the fact that the profit made in the early years was not being taxed, but that it was being used only to determine the expense for the year 1921 of the payment of interest on the bonds. This is not a tax but an allocation, under proper accounting methods for books kept on the accrual basis, of the expense chargeable to the year 1921. See Chicago, Rock Island & Pacific Ry. Co., 13 B. T. A. 989, 1029.

It may be true that the regulations of the Treasury De- [fol. 87] partment (see Article 332 of Regulations 74) are so framed as not to provide for amortization of premiums, but the Treasury regulations are founded on the law, and if the law allows this to be done the regulations cannot prevent it,—a river can rise no higher than its source.

The case of Commissioner v. Old Colony Railroad, ubi supra, is not inconsistent with the amortization of premiums for the purpose of ascertaining the expense properly chargeable to the year 1921. Compare, in this connection, Indiana Harbor Belt R. R. Co. v. Commissioner, 16 B. T. A. 279, with Terminal R. R. v. Commissioner, 17 B. T. A. 1135, 1167.

The order or decision of the Board of Tax Appeals is reversed and the case is remanded to that Board for further proceedings not inconsistent with this opinion.

On April 23, 1931, this case came on to be heard, and was fully heard by the court, Honorable George H. Bingham and Honorable Scott Wilson, Circuit Judges, and Honorable James A. Lowell, District Judge, sitting.

IN UNITED STATES CIRCUIT COURT OF APPEALS

FINAL DECREE—June 10, 1931

This cause came on to be heard April 23, 1931, upon the record upon petition for review of the United States Board of Tax Appeals and was argued by counsel:

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In failing to follow its own decision rendered in the case of the same taxpayer for the preceding calendar year (26 Fed. (2d) 408) which held, on the authority of numerous decisions of the Supreme Court, that premiums received by the taxpayer prior to the adoption of the Sixteenth Amendment were not taxable in any part for the year 1920.

2. In failing to hold that the provisions of Section 234 (a) (2) of the Revenue Act of 1921 allowing as a deduction from gross income "all interest paid or accrued within the taxable year on its indebtedness" entitle the taxpayer to a deduction of all such interest without adjustment for premiums received upon the sale of bonds prior to the adoption of the Sixteenth Amendment.

3. In making the assumption, unsupported by the record, "that the profit made in the early years was not being taxed, but that it was being used only to determine the expense for the year 1921 of the payment of interest on the bonds."

4. In holding that "the case of Commissioner *v.* Old Colony Railroad Company, supra, is not inconsistent with the amortization of premiums for the purpose of ascertaining the expense properly chargeable to the year 1921."

REASONS FOR GRANTING THE WRIT

The decision of the Circuit Court of Appeals (Bingham, Wilson and Lowell, JJ) is in direct conflict with the decision of the same Court (Bingham, Johnson and Hale, JJ) in the case of the same taxpayer for the preceding calendar year (26 Fed. (2d) 408) which held that since the premiums were received by the taxpayer prior to the adoption of the Sixteenth Amendment they were not intended by the Revenue Act of 1918 to be taxed in any part as income for 1920 and that Congress could not have

taxed them as income for 1920 had it desired to do so. The reconciliation suggested in the last opinion of the Circuit Court of Appeals between it and the first opinion is an attempt to approve the accomplishment by indirection of a result which was condemned when accomplished directly, and is accordingly out of harmony with *National Life Ins. Co.* v. *U. S.*, 277 U. S., 508 and other decisions of this court.

The last opinion of the Circuit Court of Appeals for the First Circuit is out of harmony with the opinion of the Circuit Court of Appeals for the Seventh Circuit in *Chicago, Rock Island & Pacific Railway Co.* v. *Commissioner*, 47 Fed. (2nd) 990, which relied upon the first opinion of the Circuit Court of Appeals for the First Circuit as authority for holding in favor of the Government that the cost of selling bonds prior to 1913 could not be amortized and charged as deductions in years subsequent thereto.

In petitioning to this Court for certiorari to review the first decision of the Circuit Court of Appeals, the Solicitor General stated "The question involved is one of great public importance, and vitally affects the Government in its administration of the revenue laws. It is a question which should be finally settled by this Court * * *". The question, not yet having been settled by this Court, is presumably in the same status, for it can hardly be said that a question is important when the decision of the lower court was unfavorable to the Government but unimportant when it was favorable.

The statistics (as of January 1, 1918) given by the Solicitor General in his petition in the earlier case and in his brief in support of that petition for the purpose of showing the importance of the question then raised as to the year 1920, are equally applicable in determining the importance of the same question when raised as to the year 1921.

WHEREFORE, it is respectfully submitted that this petition for writ of certiorari to review the judgment of the Circuit Court of Appeals for the First Circuit should be granted.

J. S. Y. IVINS,
Attorney for
Old Colony Railroad Company,
c/o Brewster, Ivins & Phillips,
Southern Building,
Washington, D. C.

September 4, 1931.

BRIEF

OPINION BELOW

The opinion of the Circuit Court of Appeals for the First Circuit appears in the record at page 73. It is not yet officially reported.

JURISDICTION

The final decree of the Circuit Court of Appeals was entered on June 10, 1931 (R. p. 75). The jurisdiction of this Court is invoked under section 347 of the United States Code (Act of February 13, 1925 Ch. 229 § 1).

STATEMENT

The facts are set forth in the statement in the annexed petition (p. 2, supra).

The original theory of the Government with respect to the proper treatment of premiums on bonds* for the purposes of the income tax laws, was that such premiums were in themselves income, deemed to be realized (by a taxpayer reporting income on the accrual basis) ratably over the life of the bonds. This theory was first set forth in 1919 in Treasury Regulations 45, Article 544 (2) (a) which provided:

> "If bonds are issued by a corporation at a premium, the net amount of such premium is gain or income which should be prorated or amortized over the life of the bonds."

Similar language has appeared in all income tax regulations since promulgated.

In the first Old Colony Railroad Company case (26 Fed. (2d) 408) the Circuit Court of Appeals did not deny this principle but held in effect that it was not applicable to a case where the bonds had been issued and the pre-

* i.e. the excess of the price realized by the obligor upon their original sale over their face or par value.

miums realized prior to the adoption to the Sixteenth Amendment to the Constitution, when the taxpayer kept its accounts on the basis of cash receipts and disbursements. Its decision was based on numerous opinions of this Court to the effect that property which was part of the taxpayer's capital before the Sixteenth Amendment could not be taxed as income thereafter.*

The Solicitor General filed a petition for certiorari, which was allowed (October Term 1928, No. 407) and he then filed a brief in this Court on an entirely new theory, arguing that the premiums were *not* income, but additional borrowed money, to be repaid in the form of part of the interest contracted for. Accordingly he claimed that ratable portions of the premiums should not be *added* to *income* (as the Regulations provided) but that the taxpayer's deduction from gross income for interest paid on indebtedness should be reduced each year by a ratable proportion of the premium.

On discovering that the record before this Court was insufficient to sustain his argument, the Solicitor General moved for dismissal of his writ of certiorari,† and the Government prepared to take up another case with a fuller record.

The second case of the same taxpayer (which is the present case at bar) had been tried before the Board of Tax Appeals on a record which (as far as this point is concerned) was similar to that in the first case. It was decided by the Board on November 19, 1929 in favor of

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* Lynch *v.* Turrish, 247 U. S. 221, 38 S. Ct. 537, 62 L. Ed. 1087; Southern Pacific Co. *v.* Lowe, 247 U. S. 330, 38 S. Ct. 540, 62 L. Ed. 1142; Doyle *v.* Mitchell Bros. Co., 247 U. S. 179, 38 S. Ct. 467, 62 L. Ed. 1054; Hays *v.* Gauley Mountain Coal Co., 247 U. S. 189, 38 S. Ct. 470, 62 L. Ed. 1061; Merchants' Loan & Trust Co. *v.* Smietanka, 255 U. S. 509, 41 S. Ct. 386, 65 L. Ed. 751, 15 A.L.R. 1305; Goodrich *v.* Edwards, 255 U. S. 527, 41 S. Ct. 390, 65 L. Ed. 758.

† The motion was granted April 15, 1929; 279 U. S. 876.

the taxpayer on the authority of the decision of the Circuit Court of Appeals in the first case (R. pp. 40 50). Upon joint motion of the parties* the Board's decision was vacated and further facts found in accordance with a stipulation,† to make the record show that the taxpayer had taken a deduction, from its 1921 gross income, of interest paid on indebtedness. Counsel for the Government then presented the new theory to the Board and requested reconsideration of the issues, which the Board denied on June 19, 1930.‡ The Board's original determination was reinstated as of that date.

Subsequently the Board had occasion to review the whole subject in a case where the Government presented the new and old theories in the alternative. It held that the old theory was sound, and should be applied in a case where the bonds had been issued after the adoption of the Sixteenth Amendment, distinguished the first decision of the Circuit Court of Appeals in the Old Colony Railroad 1920 case on the ground that there the bonds had been issued before the Sixteenth Amendment, *and rejected the new theory as unsound.*§

The Government took the second Old Colony Railroad case to the Circuit Court of Appeals for the First Circuit, and urged the new theory. That court (only one of the judges who had sat in the first case being present) accepted the new theory and reversed the Board.|| It distinguished its earlier decision (which had been accepted as sound in the Seventh Circuit)¶ on grounds which, we submit, are erroneous.

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* R. p. 64.

† R. p. 64.

‡ R. p. 66.

§ *Fall River Electric Light Co.* v. *Commissioner*, 23 B.T.A. 168.

|| R. p.

¶ *Chicago, Rock Island & Pacific Railway Co.* v. *Commissioner*, 47 Fed. (2d) 990.

SPECIFICATION OF ERRORS

See petition at p. 4, supra.

SUMMARY OF ARGUMENT

I. The taxpayer's bonds were sold at a premium between 1893 and 1904, when the taxpayer's accounts were kept on a cash basis. In a litigation over its 1920 income tax the same Circuit Court of Appeals (but with two different judges out of three) held that the premiums, having been part of capital before the adoption of the Sixteenth Amendment could not be taxed as income thereafter. Then the Government evolved a new theory —that instead of being *income*, the premiums were borrowed capital, to be returned as part of the interest contracted for, and that the taxpayer's deduction for interest in each year should be reduced by a ratable proportion of the premiums. This theory is in conflict with Treasury Regulations and statutory reenactments. It is also unsound, being based on circular reasoning—the conclusion being the only basis of the premise from which the conclusion is reached. The Regulations are sound, but are not applicable to a case where the premiums became capital before the Sixteenth Amendment. The opinion below shows confusion in the mind of its writer as to what the Regulations provide.

II. The statute allows the deduction from gross income of "all interest paid on indebtedness" and precludes the reduction of that deduction, even if some of the interest does constitute a capital transaction, in the same manner that estate taxes are deductible although they affect capital and not true income.

III. Because of the provisions of the lease, the taxpayer gets no benefit from the premiums until 1992, and at most could only be taxable for 1921 on the present value $6,960.64 payable in 1992, or about $445.

ARGUMENT

Point I

The Government's New Theory is Unsound

The Old Colony bonds were sold at a premium between 1893 and 1904, when the company kept its books on a cash basis.* The premiums were received at that time. In the first case the Circuit Court of Appeals held:†

> "It is not to be presumed that Congress by the act of 1918 intended to tax the whole or any part of the premiums on bonds received prior to February 25, 1913, whether the life of the bonds extended into a taxable year subsequent to February 25, 1913, or not, as it was beyond its power to do so at the time they were received."

citing the cases from this Court listed in the footnote to p. 8 supra.

Then the Government evolved its new theory.

Article 544 of Regulations 45‡ interpreted the Revenue Act of 1918. The same interpretation has been placed upon every subsequent revenue act by every subsequent edition of Treasury Department regulations.§ It is interesting to note that even after the Department of Justice had evolved its new theory and applied to this Court for certiorari in the 1920 case, the Treasury Department, under date of January 3, 1929, promulgated Regulations 74 reiterating the article which the Government's theory rejects as unsound, and that although the Treasury Department has promulgated dozens of amendments to the regulations in the last two years it has not amended this article.

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* See second paragraph of opinion below, R. p. 74.

† *Commissioner* v. *Old Colony Railroad Company*, 26 Fed. (2d) 408, 410.

‡ Quoted above, p. 7.

§ Regulations 62, Art. 545; Regulations 65, Art. 545; Regulations 69, Art. 545; Regulations 74, Art. 68.

As Mr. Justice Sutherland quoted in *Lynch* v. *Alworth Stephens Co.*, 267 U. S. 364, 370:

> "And the plain, obvious and rational meaning of a statute is always to be preferred to any curious, narrow, hidden sense that nothing but the exigency of a hard case and the ingenuity and study of an acute and powerful intellect would discover."

If the Government's new theory were obvious and rational, we might almost be justified in wondering how the Treasury Department could have kept writing and rewriting regulations for the last 12 years without discovering it. The Regulations, we submit, express the obvious and rational meaning of the statute, and they have been found satisfactory and have been approved by the Board of Tax Appeals and the Courts—as far as they go. The Circuit Court of Appeals did not hold in the first Old Colony case that Article 544 of Regulations 45 was wrong. The effect of the decision was merely to hold that the regulation had no application to premiums received before 1913. It was clear to the Court that, upon the theory which was the basis of the regulation and which had been the basis of the Government's action in all the cases involving premiums received after 1913, it was necessary to cut off the application of the regulation at the effective date of the Sixteenth Amendment, for under the theory on which the regulation was based there was a constitutional objection to taxing as income in 1920 something which had become capital* before the Sixteenth Amendment permitted the taxation, without apportionment, of income from property. But now the Government in its effort to justify a tax in 1921 on property received in 1895–1904 is ready to abandon the regulations under five successive Revenue Acts and set up in

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* Whether it ever passed through the phase of being income or not.

their place a theory which, we submit, comes within the second category of Mr. Justice Sutherland's classification, above. The Government's new theory is that

> "When the bonds in question were issued there was a rate of interest at which they could have been sold on the market at par. This rate is known as the effective rate. Because the taxpayer was willing to pay a higher rate of interest, it was able to sell them at a premium. These premiums are lump payments made in return for the obligation which the taxpayer assumed to pay such higher rate of interest during the life of the bonds. The premiums represent the present value, as of the date of sale of the bonds, of the annual payments represented by the excess interest which the taxpayer thus agreed to make during the life of the bonds. The premiums are thus repaid dollar for dollar in installments and in the form of excess interest on the face of the bonds."

This is all fine theorizing but it is not based on a single known demonstrable fact either in the record or elsewhere. John Dewey, in "Experience and Nature," says:

> "Systems have always worked with loaded dice; their premises have been framed to yield desired conclusions."

The Government takes for its major premise the proposition that "when the bonds in question were issued there was a rate of interest at which they could have been sold on the market at par." We are certainly entitled to be told what the Government claims that rate, which it calls "the effective rate," to have been. Only thus will we be in a position to verify by mathematics whether the conclusion does follow from the premise. But we should not be asked to determine the rate which is to constitute the premise, by reasoning backward from the conclusion.

The factors going to determine the price at which a bond will sell are legion. The rate of interest offered is,

a part of the interest deducuon allowed under Section 234 (a) (2) of the Revenue Act of 1921?

The Board of Tax Appeals has answered this question in the negative in two cases litigated between the Old Colony Railroad Company and the Commissioner of Internal Revenue.* The Circuit Court of Appeals for the First Circuit (Circuit Judges Bingham and Johnson and District Judge Hale) affirmed the first decision of the Board of Tax Appeals (26 Fed. (2d) 408). The same court (Circuit Judges Bingham and Wilson and District Judge Lowell) reversed the Board in the second case (R. p. 73).

This court on the petition of the Solicitor General allowed a writ of certiorari in the first case (October Term, 1928, No. 407) but the writ was dismissed on the Solicitor General's motion.

The taxpayer now seeks to review the second decision of the Circuit Court of Appeals, urging grounds similar to those presented by the Government in support of the petition to review the first decision.

STATEMENT

Between 1895 and 1904, while all the taxpayer's property was under lease to The New York, New Haven and Hartford Railroad Company, bonds were issued in the name of the taxpayer which were sold at a premium in excess of their face amount, aggregating $199,528.08. At this time the taxpayer's books were kept on a cash payment basis. In [illegible], the Interstate Commerce Commission required the taxpayer, for the purpose of its reports to that Commission, to amortize the premiums over the periods of the respective lives of the bonds. Under protest, the taxpayer for each year subsequent to 1914 reported to the Interstate Commerce Commission a portion of such premiums as income. But on its books it credited such proportion to Profit and Loss account (a

*6 B.T.A. 1025, and 18 B.T.A. 267, 275.

surplus account) and not to its Income account. The amount so credited to Profit and Loss account for 1921 was $6,960.64.

The taxpayer, having received no part of this $6,960.64 in 1921 and being unable (because of the lease) to receive any benefit from the fact that the bonds had been sold at a premium until the termination of the lease in 1992, did not include the $6,960.64 as part of its taxable income in its income tax return for 1921 filed with the Treasury Department.

In auditing that income tax return, the Commissioner of Internal Revenue increased the taxpayer's taxable income for the year 1921 by such amount of $6,960.64 and proposed to assess a deficiency tax accordingly. The Board of Tax Appeals, on the authority of its decision in the case of the same taxpayer for the preceding tax year (*Old Colony Railroad Company* v. *Commissioner*, 6 B.T.A. 1025) and the affirmance of that decision by the Circuit Court of Appeals for the First Circuit (26 Fed. (2d) 408), held that no part of the premiums in question represented income to the petitioner in 1921. Subsequently, the Commissioner moved the Board for reargument and reconsideration, and presented to the Board further arguments directed to the question whether the portion of the bond premiums treated by the Commissioner as income should not be given consideration in determining the interest deduction of the taxpayer for the purpose of determining its net taxable income. After consideration of this argument, the Board of Tax Appeals reinstated its order of redetermination holding that the taxpayer's net taxable income for 1921 should not be increased by reason of the premiums received between 1895 and 1904 on the sale of its bonds.

This decision of the Board of Tax Appeals was reversed by the Circuit Court of Appeals for the First Circuit in an opinion rendered June 10, 1913, per Lowell, D.J.

of Appeals in the first Old Colony Railroad case (which is not overruled in the decision we seek to review and which was accepted as sound in the Seventh Circuit) **there was no intent to tax as income something which was capital of the taxpayer before the Sixteenth Amendment.**

Judge Lowell, writing the opinion below, was apparently much confused as to what the Regulations do provide. In the last paragraph but two of the opinion (R. p. 75) he assumes that they do not provide for amortization of premiums, and that they attempt to prevent it. But they do provide for such amortization **by the process of treating the premiums as income**—and accordingly are applicable in all cases where the premiums had not become capital before the adoption of the Sixteenth Amendment.

Point II

The Statutory Provision for the Deduction from Gross Income of All Interest Paid on Indebtedness, Precludes the Application of the Government's New Theory

Section 234 of the Revenue Act of 1921 provides:

> "(a) That in computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions—
>
> " * * * (2) **All interest** paid or accrued within the taxable year on its indebtedness." (Emphasis supplied)

The statute says nothing about "effective rates" of interest paid, but **"all interest."** It must be interpreted in the light of the commonly accepted meaning of the term "interest."

The bonds in the present case, outstanding in 1921, called for the payment of $538,920 interest. The New Haven, under the lease, undertook to pay "the interest

on the lessor's bonded indebtedness" (R. 20). If the New Haven had failed to pay $6,960.64 of the $538,920 called for in the bonds, could it claim that it had not defaulted under its covenant to pay interest? Could it pay the full $538,920 but charge $6,960.64 to the Old Colony as a payment of principal, and call upon the Old Colony to issue new bonds to refund it as principal indebtedness? We do not believe that any court would so hold.

The Government made a very similar argument in *United States* v. *Woodward*, 256 U. S. 632. Section 214 (a) of the Revenue Act of 1918 provided for the deduction from gross income of "taxes paid or accrued" with specified exceptions. The Government contended that the estate tax was not a "tax" within the meaning of Section 214 (a), because it was in reality a segregation of part of the estate which was prevented from passing to the executor—a partial escheat. It also contended that the estate tax was a capital transaction, not affecting true income, but merely reducing a capital receipt of a type specifically excluded from taxable income. This Court readily disposed of both contentions on the ground that the estate tax was designated as a "tax" in the act imposing it, and that it was imposed in the exertion of the taxing power of the United States. It therefore came within the provision allowing the deduction of taxes.

The Court did not bother to answer the argument with respect to the capital nature of the estate tax, except by saying that it did not constitute a segregation but was a charge against the estate.

But the capital nature of the transaction would not prevent a deduction in the computation of net income, if Congress elected specifically to allow it as a deduction. If a capital asset is destroyed by casualty, the loss does not actually affect income, any more than does a gift. However, Congress permits the deduction of capital

losses due to casualty* but does not permit the deduction of gifts out of capital, though the effect on the taxpayer's capital, and lack of effect on his income is the same in each case.

Congress has allowed the deduction of "all interest" which precludes any argument as to whether part of the interest paid is properly a capital transaction. If the payment was "interest," it is a proper deduction—"all" of it, and not merely the "effective rate."

The transactions in this case were of the commonest kind. The Old Colony, in issuing bonds at an interest rate which would cause them to sell at a premium can hardly be accused of fraudulent intent to evade an income tax, enacted many years later. In the absence of fraud, we should interpret the language of the bonds in the sense in which it was undoubtedly understood by the parties, would commonly be understood among men—that is, that the payments, required to be made as "interest," were "interest" in the commonly accepted meaning of the word.

Point III

Even If the Government's New Theory Were Sound, It Would not be Applicable to the Present Case, Where the Interest on the Taxpayer's Bonds Was Paid By Its Lessee

The properties of the Old Colony, including the proceeds, both face amount and premium, of the bonds sold, were under lease to the New Haven for a term which, unless sooner ended by some highly improbable event, would run until 1992. The proceeds of the bonds were presumably used as provided in the lease (R. 18), for the purpose of making permanent improvements upon the property demised or for the purpose of discharging the Old Colony's indebtedness. If it was spent for im-

* cf. Revenue Act of 1921, § 214 (a) (6).

provements, the New Haven would have the benefit of the improvements until 1992. If it went to reduce indebtedness, the New Haven would be similarly benefited until 1992, for by the lease it undertook to carry the Old Colony's funded indebtedness along, refunding and paying interest as necessary, and to assume and pay all the other obligations of the Old Colony. The receipt of the premiums during the term of the lease was like an increment in the value of the real property demised. It could not benefit the lessor until the termination of the lease.

On an accrual basis, the Government might be justified in treating as income to the Old Colony in 1921 the present value in that year of the right to $6,960.64 receivable in 1992, which on a 4% compound discount basis would be about $445. But in order to justify even this adjustment to the Old Colony's income, the Government must sustain the soundness of its theory. If the Government's theory be sound, it is applicable to the Old Colony at best only to the extent of an increase in 1921 income of about $445. If it be unsound, of course it cannot justify even that adjustment.

It should be noted that although this argument was presented to the court below, the opinion makes no attempt to meet it.

Conclusion

The writ should be allowed as prayed for in the petition.

Respectfully submitted,

JAMES S. Y. IVINS,
Attorney for
Old Colony Railroad Company.

September 4, 1931.